

Message Text

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FM AMEMBASSY KATHMANDU

TO SEDSTATE WASHDC 9907

INFO AMEMBASSY DACCA

AMEMBASSY MOSCOW

AMEMBASSY NEW DELHI

AMCONSUL CALCUTTA

AMCONSUL HONG KONG

USLO PEKING

CINCPAC

C O N F I D E N T I A L SECTION 1 OF 4 KATHMANDU 4540

LIMDIS

E.O. 11652: GDS

TAGS: PFOR, PINS, NP, US

SUBJECT: NEPAL: CURRENT SITUATION

REF: KATHMANDU 2953

1. SUMMARY: AS WE REPORTED LAST JULY, THERE IS A CONTINUING MALAISE IN KATHMANDU. DISSATISFACTION WITH THE KING'S LEADERSHIP AND THE PANCHAYAT SYSTEM REMAINS. THE KATHMANDU INTELLIGENTSIA AND TERAJ BUSINESSMEN CRITICIZE THE PRESENT SYSTEM FOR ITS INCAPACITY TO (A) HANDLE THE CURRENT ECONOMIC CRISIS, (B) CHECK CORRUPTION AND NEPOTISM, AND (C) PROVIDE THE DEGREE OF POLITICAL PARTICIPATION NECESSARY TO MEET THE RISING EXPECTATIONS OF THE MASSES. THIS DISSATISFACTION POSES NO IMMEDIATE THREAT TO THE REGIME, BUT THERE IS LIKELY TO BE A CONTINUING LAW AND ORDER PROBLEM AND POSSIBLY A FURTHER EROSION OF PUBLIC CONFIDENCE IN THE SYSTEM AS IT IS
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PRESENTLY CONSTITUTED. THE KING HAS FEW ECONOMIC OPTIONS

OPEN TO HIM GIVEN THE DEPENDENCE OF THE ECONOMY ON NEIGHBORING INDIA. THE CORONATION, HOWEVER, WILL, FOR A TIME, DISTRACT ATTENTION FROM OTHER MORE PRESSING PROBLEMS, THOUGH THE OPPOSITION, PARTICULARLY ITS EXILE WING, MAY SEEK TO DISRUPT THE CORONATION PREPARATIONS IN ORDER TO FOCUS ATTENTION ON THE KINGDOM'S POLITICAL PROBLEMS. AFTER THE SEVERE DETERIORATION IN INDO-NEPALESE RELATIONS IN LATE SUMMER, THE GON SEEMS TO BE SEEKING A MORE BALANCED RELATIONSHIP WITH INDIA AND A RETURN TO GREATER NORMALCY. IN THE FACE OF THESE UNCERTAINTIES, DOMESTIC AND EXTERNAL, U.S. PROGRAMS CONTINUE TO BE SEEN AS A STABILIZING FACTOR. END SUMMARY.

2. THE POLITICAL SITUATION: A NOTEWORTHY FEATURE OF POLITICAL ACTIVITY IN KATHMANDU IN RECENT MONTHS HAS BEEN A MORE ACTIVE DEBATE ON THE QUESTION OF POLITICAL REFORM. ON THE ONE HAND ARE THOSE PALACE ADVISORS AND PANCHAYAT MEMBERS WHO CLAIM THAT ANY ALTERATION IN THE SYSTEM WILL OPEN THE FLOOD GATES; POLITICAL PARTIES WILL RETURN, AND B.P. KOIRALA WILL BE KNOCKING AT THE GATES OF KATHMANDU. THE OTHER SIDE, HOWEVER, ARGUES EQUALLY VEHEMENTLY THAT NOT TO ADOPT SOME MODICUM OF REFORM WILL SIMPLY DRIVE THE DISENCHANTED INTO THE ARMS OF VIOLENT REVOLUTIONARIES WHO HAVE OPENLY ESPOUSED TERRORISM.

3. THIS OPEN DEBATE HAS GIVEN RISE TO A NUMBER OF POLITICAL GROUPINGS, THE MOST IMPORTANT OF WHICH IS THE ONE NOMINALLY GATHERED AROUND T.P. ACHARYA (BUT IN REALITY INSPIRED BY RISHIKESH SHAHA), WHICH WHILE CLAIMING NO PARTICULAR IDEOLOGY, IS WILLING TO ADMIT THE POSSIBILITY THAT THE WHOLE PANCHAYAT SYSTEM SHOULD BE JUNKED AND THE WAY OPENED FOR A MULTI-PARTY SYSTEM WITHIN A FRAMEWORK OF CONSTITUTIONAL MONARCHY. THE PRESIDENT OF THE EXILED NEPALI CONGRESS PARTY, GENERAL SUBARNA SHUMSHER, ON THE OTHER HAND, HAS TRIED TO ATTRACT THOSE MODERATES WHO, WHILE ADHERING TO THE BASIC TENETS OF THE PANCHAYAT SYSTEM, ARE PRESSING FOR THE SO-CALLED "TRIUMVIRATE REFORMS," I.E., PUBLIC SESSIONS OF THE PANCHAYAT, DIRECT ELECTIONS BASED ON BROAD SUFFRAGE, AND ELECTION OF THE PRIME MINISTER BY THE NATIONAL PANCHAYAT. TO DATE THE PALACE HAS GIVEN NO INDICATION WHETHER IT WILL ADOPT ANY OF THESE POLITICAL SUGGESTIONS, BUT THE BETTING CONFIDENTIAL

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APPEARS TO BE THAT H.M. WILL INTRODUCE SOME REFORMS. PRIME MINISTER RIJAL, WHO HAS HIS OWN OBVIOUS AXE TO GRIND, SUGGESTED AT A RECENT MEETING OF THE BACK TO THE VILLAGE CAMPAIGN, THAT HE, IN ANY CASE, WOULD OPPOSE A REFORM WHICH WENT SO FAR AS TO MAKE THE PM BEHOLDEN TO THE PANCHAYAT, AND THIS VIEW PROBABLY REPRESENTS PALACE THINKING.

4. BEHIND MUCH OF THE RHETORIC, HOWEVER, IS THE QUESTION

OF HOW THE PALACE WILL WOLVE THE PROBLEM OF THE STILL
INDISTINCT LINES OF AUTHORITY. AT THE MOMENT FEW OFFICIALS
CAN BE SURE THAT THEIR DAY TO DAY ADMINISTRATIVE DECISIONS
WILL NOT SUBSEQUENTLY BE OVERRULED BY A PALACE ADVISOR.
AS A RESULT A FEELING OF LASSITUDE IS GRADUALLY MAKING ITS
WAY FELT AMONG BROAD SEGMENTS OF THE SOCIETY. BIRENDRA HAS
NOT MADE THE IMPACT MANY HAD HOPED HE WOULD, AND ONE HEARS
MORE AND MORE TALK ABOUT HIS BEING CUT OFF FROM THE
COUNTRY'S "REAL PROBLEMS."

5. ALL THIS IS NOT TO IMPLY THAT THE PUBLIC ARE HOSTILE OR
WILLING TO SUPPORT THE TERRORIST ACTIVITIES OF THE EXILED
NEPALI CONGRESS OR MAOIST GROUPS. PRESENT POLITICAL DISSENT,
EVEN THAT OF ACHARYA, APPEARS WELL WITHIN THE BOUNDARIES OF
WHAT THE PALACE WILL TOLERATE. BUT THE PALACE DOHL SET
BOUNDARIES AND IS CONCERNED TO ARM ITSELF AGAINST THE
POSSIBILITY OF INCREASED TERRORIST ACTIVITY. THE RECENT
MOVE OF SOME PANCHAYAT MEMBERS PETITIONING THE KING TO
PROMULGATE A DECREE GRANTING ZONAL COMMISSIONERS THE POWER
TO TRY TERRORISTS AND CARRY OUT THE DEATH PENALTY IS A STEP
IN THIS DIRECTION. ON OCTOBER 18 A DECREE WAS ISSUED WHICH
WILL ESTABLISH "SPECIAL COURTS," AND ALTHOUGH THE DETAILS
REMAIN UNKNOWN, THE COURTS WILL PRESUMABLY DEAL WITH TERRORISTS.

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6. THE THREAT TO LAW AND ORDER PRESENTLY POSED BY THE NCP EXILES REMAINS. WHILE FEW BELIEVE THAT B.P. KOIRALA HAS SUFFICIENT STRENGTH TO ORGANIZE A REALLY EFFECTIVE OPPOSITION TO THE GOVERNMENT, HE CERTAINLY HAS THE CAPACITY TO KEEP THE PRESSURE ON KATHMANDU IN THE PERIOD BEFORE THE CORONATION. HE IS A POTENT POLITICAL SYMBOL AND HIS CHARISMA IS UNIQUE AMONG NEPALI POLITICIANS; AS SUCH THE GOVERNMENT HAS BEEN AT PAINS TO DISCREDIT HIM, MOST RECENTLY BY BRINGING A CASE FOR TERRORISM AGAINST HIM IN ABSENTIA. GRENADE AND OTHER MINOR TERRORIST ACTIVITY SEEMS TO HAVE DIMINISHED IN RECENT MONTHS BUT IT MAY INCREASE AS THE CORONATION APPROACHES. IF, HOWEVER, INDIA CONTINUES TO RESTRAIN HIS ACTIVITIES AND THE RESIDENT OPPOSITION IN NEPAL REMAINS FRAGMENTED, THERE SEEMS LITTLE PROSPECT THAT KOIRALA AND THE NCP WILL BECOME MORE THAN AN IRRITANT TO HMG.

7. IN SUM, THE KING APPEARS TO FEEL RELATIVELY SECURE. HE HAS ALLOWED OPEN DEBATE WITHIN LIMITS AND INDEED WILL PROVOKE IT, AS HE DID BY HIS MEETING WITH FORMER PRIME MINISTERS TO
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SOLICIT THEIR VIEWS ON WHAT DIRECTION REFORM SHOULD TAKE. AT THIS STAGE OF NEPAL'S POLITICAL DEVELOPMENT, IT SEEMS PROBABLE THAT REFORM WILL BE PROMULGATED AT THE KING'S PLEASURE, NOT IN RESPONSE TO PRESSURE FROM BELOW.

8. FOREIGN POLICY: IN THE MONTHS PRIOR TO INDIA'S "ASSOCIATION" OF SIKKIM, MANY NEPALIS BELIEVED THAT INDIA WAS MAKING GENUINE EFFORTS TO REDUCE THE BILATERAL DIFFERENCES WHICH ARE BOUND TO EXIST IN ANY RELATIONSHIP AS BROAD AS THAT BETWEEN INDIA AND NEPAL. MOST NEPALIS HOPED THAT THE GOI HAD PLACED "GENUINE" RESTRICTIONS ON B.P. KOIRALA AND OTHER EXILED NEPALI CONGRESS PARTY ACTIVISTS, AND THEY WELCOMED INDIA'S TACIT SUPPORT FOR THE POLITICAL QUO. NOW THEY ARE NOT SO SURE.

9. FRIENDLY RELATIONS WITH INDIA, THE LINCHPIN OF NEPAL'S FOREIGN POLICY IF NOT OF ITS EXISTENCE AS AN INDEPENDENT STATE, HAVE BEEN JARRED IN THE AFTERMATH OF THE SIKKIM AFFAIR. TRADITIONAL FEELINGS OF UNEASINESS HAVE BEEN EXACERBATED BY WHAT NEPAL VIEWS AS PRECIPITIOUS GOI REACTION TO THE KATHMANDU DEMONSTRATIONS (WHILE THE INDIANS SEE AS AN OVER-REACTION TO THE SIKKIM EVENTS). THERE ARE FEW WHO WILL PREDICT WITH ANY CONFIDENCE WHAT WILL RESULT FROM DELHI'S "OVERALL REVIEW" OF BILATERAL RELATIONS.

10. IN THE DAYS FOLLOWING THE RECALL OF INDIAN AMBASSADOR

RASGOTRA SOME GON OFFICIALS WERE GENUINELY CONCERNED THAT THINGS HAD GOTTEN OUT OF HAND AND A CONCERTED EFFORT WAS MADE TO NARROW THE GROWING RIFT BETWEEN KATHMANDU AND DELHI. EVEN NOW AFTER RASGOTRA'S RETURN, BOTH SIDES REMAIN CHARY OF EACH OTHER'S ACTIONS AND MOTIVES. THE GON REMAINS UNCERTAIN WHAT WILL RESULT FROM DELHI'S "REVIEW" AND WHAT MESSAGE RASGOTRA HAS BROUGHT BACK: A REDUCTION IN ECONOMIC ASSISTANCE, A THREAT TO UNLEASH THE NCP, OR A WILLINGNESS TO LET BYGONES BE BYGONES. WE ASSUME THAT IN FACT THERE WILL BE LITTLE MORE THAN TOUGH TALK FOR THE TIME BEING AND THAT EFFORTS MAY BE MADE TO PATCH UP THE RELATIONSHIP. WITH THIS END IN MIND THE NEPALESE ARE KNOWN TO BE URGING A VISIT TO KATHMANDU OF THE INDIAN FOREIGN SECRETARY.

11. ALTHOUGH MOST NEPALIS RECOGNIZE THE NEED TO MAINTAIN GOOD RELATIONS WITH DELHI (IF ONLY FOR ECONOMIC SURVIVAL)
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MANY ARE DISTURBED BY INDIA'S NEW ASSERTIVENESS. THERE ARE THOSE IN HIGH GOVERNMENT POSITIONS WHO CLAIM TO SEE A SINISTER CONTINUUM IN INDIAN FOREIGN POLICY WHICH CAN BE TRACED FROM HYDERABAD IN 1950 THROUGH THE 1971 INDO-PAK WAR TO SIKKIM. INDIA'S DECISION TO BECOME A NUCLEAR POWER WAS IN ITSELF ALARMING, BUT THE DECISION TO "ANNEX" A NEIGHBORING MONARCHICAL STATE HIT FAR CLOSER TO HOME.

12. BY AND LARGE NEPAL FEELS CONFIDENT THAT IT CAN HANDLE ANY MINOR SHIFT IN THE RELATIONSHIP WITH DELHI. IRRITANTS IN THE TRADE AND AID RELATIONSHIP CAN ALSO BE EXPECTED TO CONTINUE AND THE CURRENT INFLUX OF INDIANS FROM BIHAR AND U.P. INTO THE TERAJ IS ALSO LIKELY TO CREATE CONSIDERABLE FRICTION, BUT AT TOLERABLE LEVELS. WHAT REALLY DISTURBS THE GON AND THE PALACE IS THE QUESTION WHETHER OR NOT INDIA WILL ALTER ITS TACTICAL SUPPORT FOR THE MONARCHY AND THE PRESENT POLITICAL SYSTEM. ALTHOUGH SUCH A DECISION STRIKES US AS UNLIKELY IT IS AN OPTION, LIKE ECONOMIC PRESSURE, WHICH INDIA WILL PRESUMABLY KEEP OPEN.

13. IF NEPAL IS SUSPICIOUS OF INDIA, INDIA IS EQUALLY SUSPICIOUS OF CHINA'S INFLUENCE IN KATHMANDU. THERE IS NO QUESTION THAT THE PRC CONTINUES TO PLAY AN ACTIVE, IF MUHD, ROLE; HER VISIBLE AID PROJECTS ARE A DAILY REMINDER THAT CHINA, WHILE NO REAL ALTERNATIVE TO INDIA, IS AN IMPORTANT BALANCE TO DELHI'S POWER. IN RECENT WEEKS NEPAL HAS NOT HESITATED TO PLAY UP THE IMPORTANCE OF THE PRC, AND CONSIDERABLE PUBLICITY WAS GENERATED DURING THE 25TH ANNIVERSARY CELEBRATIONS OF THE PRC. WE HAVE THE IMPRESSION, HOWEVER, THAT CHINA HAS BEEN CIRCUMSPECT OVER THE SIKKIM ISSUE, CAREFUL NOT TO INJECT ITSELF DIRECTLY INTO THE CURRENT DISPUTE BETWEEN KATHMANDU AND DELHI. IT HAS PLAYED THE ROLE

OF A SYMPATHETIC NEIGHBOR, HOPEFUL OF FOSTERING THE IMAGE OF A
GUARANTOR OF NEPALESE SOVEREIGNTY BY VIRTUE OF ITS
GEOGRAPHIC POSITION, RATHER THAN BY OVERT ACTION.

14. AS FOR THE SOVIET UNION ITS RELATIONSHIP WITH INDIA HAS
REDUCED ITS EFFECTIVENESS AS A "DISINTERESTED OBSERVER."
BY AND LARGE MOST NEPALIS REALIZE THAT THE SOVIETS HAVE BIGGER
FISH TO FRY AND THAT, DESPITE THE VISIT TO MOSCOW BY MINISTER
OF STATE FOR FINANCE BHEKH THAPA, NEPAL DOES NOT RANK HIGH IN THE
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PRIORITIES FOR SOVIET DEVELOPMENT RESOURCES.

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INFO AMEMBASSY DA CCA
AMEMBASSY MOSCOW
AMEMBASSY NEW DELHI
AMCONSUL CALCUTTA
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15. ALTHOUGH NEPAL CONTINUES TO PLAY AN ACTIVE ROLE IN THE
NON-ALIGNED MOVEMENT, THERE ARE SOME INDICATIONS THAT THE MFA
PROFESSIONALS ARE BECOMING LESS SANGUINE ABOUT WHAT NEPAL

CAN EXPECT FROM ITS THIRD WORLD FRIENDS. SUPPORT FOR NEPAL'S POSITION AT THE CARACAS LOS CONFERENCE WAS NOT AS WIDESPREAD AS HAD BEEN HOPED, AND THERE IS LITTLE PROSPECT THAT THE ARAB AND OPEC NATIONS WILL HELP TO EASE NEPAL'S ENERGY CRISIS. DESPITE THESE DISAPPOINTMENTS IT IS UNLIKELY THAT THE GON ATTITUDES TOWARD THE NON-ALIGNED WILL SHIFT SIGNIFICANTLY, AND ON MOST ISSUES IT WILL GO ALONG WITH NON-ALIGNED CONSENSUS. AS A SMALL NATION BETWEEN TWO GIANTS, NEPAL WILL USE THE NON-ALIGNED STANCE TO FOSTER ITS POLICY OF SEEKING COUNTERBALANCES TO INDIAN AND CHINESE INFLUENCE.

16. ECONOMIC SITUATION: ECONOMIC PROBLEMS HAVE BECOME A MAJOR CONTRIBUTING FACTOR IN POLITICAL RESTLESSNESS. TO A LARGE EXTENT PRESENT DISSATISFACTION REFLECTS RISING EXPECTATIONS, ENGENDERED BY THE REAL, IF LIMITED, ECONOMIC AND SOCIAL PROGRESS OF RECENT YEARS. NOT UNEXPECTEDLY, PEOPLE

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ARE IMPATIENT; THERE HAVE BEEN HEATED DEBATES IN THE PANCHAYAT OVER ECONOMIC PROBLEMS; AND NEPALIS ARE BECOMING INCREASINGLY DISGRUNTLED OVER THE APPARENT INABILITY OF THE GON TO ACT IN THE FACE OF INFLATION AND SHORTAGES WHICH BY NOW HAVE AFFECTED EVERY NEPALI.

17. WHILE THERE ARE STRUCTURAL PROBLEMS WHICH MAY BE MORE DAMAGING TO NEPAL'S ECONOMY, THE MOST VISIBLE AND EMOTIONAL PROBLEMS ARE INFLATION AND THE LACK OF CONSUMER GOODS. IN THE BEST OF CIRCUMSTANCES NEPAL'S CITIZENS LIVE CLOSE TO THE MARGIN. FOR MANY, RISING PRICES AND SHORTAGES HAVE MADE AN ALREADY MARGINAL EXISTENCE EVEN MORE MARGINAL. WHILE PRICE INDICES IN NEPAL ARE NOT ACCURATE, CENTRAL BANK FIGURES INDICATE THAT PRICES HAVE INCREASED ON AVERAGE APPROXIMATELY 20 PERCENT OVER THE LAST YEAR. UNFORTUNATELY, PRICE INCREASES FOR SOME ESSENTIAL FOOD ITEMS AND COMMODITIES HAVE BEEN MUCH GREATER. IN KATHMANDU FOR EXAMPLE PRICES OF VEGETABLE OILS, GHEE, MEAT AND POUPDRY PRODUCTS HAVE RISEN BY ONE THIRD, WITH PRICES FOR VEGETABLES AND SPICES UP BY NEARLY ONE HALF.

18. INCREASES IN COSTS OF CONSTRUCTION MATERIALS HAVE HAD A SEVERE EFFECT ON NEPAL'S DEVELOPMENT EFFORTS. PRICES FOR CEMENT, BRICKS, GASOLINE, AND OIL HAVE ALL RISEN CONSIDERABLY. IN SOME CASES THIS HAS NECESSITATED CHANGES IN GOVERNMENT AND FOREIGN DONOR DEVELOPMENT PROJECTS, SUCH AS THE SURKHET ROAD, WHERE ESCALATING COSTS HAVE LED TO REASSESSMENTS. THE PROBLEM OF SCARCITIES HAS BEEN EQUALLY SEVERE, WITH SOME COMMODITIES BEING UNAVAILABLE, REGARDLESS OF COST, IN SUFFICIENT QUANTITIES. NUMEROUS CONSTRUCTION PROJECTS HAVE BEEN DELAYED OR HALTED DUE TO SHORTAGES OF CEMENT AND BRICKS. PETROLEUM PRODUCTS CONTINUE TO BE IN SHORT SUPPLY. OF EVEN MORE IMPORTANCE TO THE AVERAGE NEPALI IS THE SHORTAGE OF

KEROSENE WHICH IS NEEDED FOR COOKING. SIMILARLY, VEGETABLE OILS ALSO NEEDED FOR COOKING HAVE BEEN IN SHORT SUPPLY, NECESSITATING RATIONING.

19. THE GON IS FRUSTRATED BECAUSE THERE IS LITTLE IT CAN DO ABOUT MOST OF THE INFLATIONARY PRESSURES. THE RISING COST OF IMPORTS IS INFLUENCED BY EXTERNAL FACTORS OVER WHICH NEPAL HAS NO CONTROL. AS MOST IMPORTS COME FROM INDIA, PRICES IN INDIA HAVE A MAJOR IMPACT ON NEPAL'S ECONOMY. IN
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ADDITION TO THE DIRECT COST OF IMPORTS, NEPAL'S ECONOMY IS INDIRECTLY AFFECTED BY THE PRICE STRUCTURE PREVAILING IN INDIA FOR FOODSTUFFS. GIVEN THE OPEN BORDER WITH INDIA, AND THE NATURAL TENDENCY OF NEPALESE FOOD PRODUCTION TO SEEK THE HIGHEST PRICED MARKETS, THE PRICE OF NEPALESE AGRICULTURAL PRODUCTS, MOST OF WHICH COME FROM THE TERAJ AREA CONTIGUOUS TO INDIA, IS SET TO A LARGE EXTENT BY PRICES PREVAILING IN INDIAN MARKETS.

20. THE GON IS NOT WITHOUT A CAPACITY TO INFLUENCE THE RATE OF INFLATION AND PARADOXICALLY HAS ALLOWED MONEY SUPPLY TO INCREASE BY ABOUT ONE THIRD IN THE LAST YEAR; HOWEVER, FUNDAMENTALLY, THE GON CONTROLS ONLY A LIMITED NUMBER OF THE BASIC FACTORS AFFECTING THE ECONOMY. AND THOSE FACTORS WHICH IT CAN CONTROL ARE BEING SUBJECTED TO INCREASING PRESSURES. WHEREAS NEPAL'S BUDGET WAS CUSTOMARILY FORMERLY IN SURPLUS, THE LAST THREE BUDGETS HAVE BEEN IN DEFICIT. EXPENDITURES WILL CONTINUE TO INCREASE AT A MORE RAPID RATE THAN REVENUES, AS THE PACE OF DEVELOPMENT DEMANDS GREATER FINANCIAL OUTPUT BY THE GON. TO CITE JUST TWO EXAMPLES, THE EDUCATION REFORM BEGUN IN 1972 REQUIRES A CONTINUING HIGH LEVEL OF EXPENDITURES, AND MAINTENANCE EXPENDITURES FOR INFRASTRUCTURE PROJECTS COMPLETED BY FOREIGN AID DONORS ARE CREATING ADDITIONAL PRESSURES. THE PAST SUMMER HAS WITNESSED THE WORST DAMAGE IN HISTORY TO NEPAL'S ROADS AS A RESULT OF HEAVY RAINS. THE TOTAL IMPACT OF THIS DEVELOPMENT IS THAT THE GON WILL BE EXTREMELY HARD PRESSED TO MOBILIZE SUFFICIENT RESOURCES TO MEET ITS FINANCIAL OBLIGATIONS.

21. WHILE INFLATION AND SHORTAGES ARE THE MOST VISIBLE PROBLEMS, THE STRUCTURAL PROBLEM CAUSING THE MOST CONCERN IS THE STAGNATION OF NEPAL'S PRODUCTION IN THE FACE OF AN INCREASING POPULATION. OFFICIAL FIGURES INDICATE THAT THE REAL RATE OF GROWTH OF NEPAL'S GROSS DOMESTIC PRODUCT IS ONLY TWO PERCENT PER YEAR, WHICH IS LESS THAN THE RATE OF POPULATION INCREASE. AS NEPAL IS PREDOMINANTLY AN AGRICULTURAL ECONOMY, IT FOLLOWS THAT AGRICULTURAL PRODUCTION IS NOT KEEPING PACE WITH POPULATION GROWTH. DESPITE CONTINUING EFFORTS BY THE GON AND FOREIGN AID DONORS, NEPAL'S AGRICULTURE IS STILL

CHARACTERIZED TO A LARGE EXTENT BY PRIMITIVE PRACTICES.
INCREASING POPULATION PRESSURES ON LAND USE CAN ONLY LEAD TO
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FURTHER SET-BACKS AS DEFORESTATION AND EROSION DECREASE NEPAL'S
PRODUCTIVE CAPACITY.

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RSC-01 /056 W
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R 061000Z NOV 74
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22. NEPAL'S INCREASING POPULATION AND THE ATTENDANT MOVE-
MENT OF PEOPLE FROM THE HILL AREAS TO THE TERA I HAS ANOTHER
OMINOUS DIMENSION. NEPAL IS DEPENDENT ON INDIA FOR MOST OF
ITS IMPORTS. TRADITIONALLY, NEPAL HAS PAID FOR THESE IMPORTS
WITH IC EARNINGS FROM SURPLUS AGRICULTURAL PRODUCTION IN THE
TERAI. WITH DOMESTIC NEEDS NOW REQUIRING AN EVER-INCREASING
PROPORTION OF THE TERA I'S AGRICULTURAL PRODUCTION, THERE IS
SERIOUS CONCERN OVER HOW IN THE FUTURE NEPAL WILL BE ABLE
TO PAY FOR ITS IMPORTS FROM INDIA. THIS STRAIN IS ALREADY

EVIDENT. WHILE THE LEVEL OF CONVERTIBLE FOREIGN EXCHANGE RESERVES REMAINS HIGH, ABOUT \$105 MILLION, AND CAN BE USED TO SOME EXTENT TO PURCHASE IMPORT NEEDS FROM OVERSEAS SOURCES, THE DEFICIENCY IN IC RESERVES IS EVEN NOW BEING FELT. THE PRESENT LEVEL OF IC RESERVES, APPROXIMATELY RS. 169 MILLION, IS SUFFICIENT TO COVER NO MORE THAN TWO OR THREE MONTHS OF IMPORTS FROM INDIA.

23. IN REVIEWING THE OVERALL SITUATION IN NEPAL, ONE CANNOT

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HELP BUT NOTE THE GROWING IMPORTANCE OF THE ECONOMY TONEPAL'S POLITICAL STABILITY. WHEREAS IN THE PAST THE GOVERNMENT OPERATED INDEPENDENTLY OF NEPAL'S PRIMITIVE NEAR-SUBSTANCE ECONOMY, CIRCUMSTANCES HAVE CHANGED. NEPAL IS NOW FAR ENOUGH INTO THE DEVELOPMENT PROCESS SO THAT PEOPLE, PARTICULARLY IN URBAN AREAS, HAVE NEW AND RISING EXPECTATIONS. THESE THE GOVERNMENT MUST TAKE INTO ACCOUNT AND TRY TO DEVELOP A COURSE OF ACTION AIMED AT IMPROVING, AT LEAST TO A LIMITED EXTENT, THE GENERAL STANDARD OF LIVING. FAILURE TO DO SO WILL ADD CONSIDERABLY TO THE GROWING DCUSATISFACTION WITH THE PANCHAYAT SYSTEM AS PRESENTLY CONSTITUTED.

24. THE U.S. ROLE: IN A PERIOD IN WHICH SERIOUS TENSIONS WITH INDIA HAVE BEEN ADDED TO LONG STANDING ECONOMIC AND POLITICAL PROBLEMS, THE ROLE OF THIRD PARTIES TAKES ON INCREASED SIGNIFICANCE. THE U.S. PRESENCE AND PROGRAMS ARE SEEN, BY THE PALACE AND GON BUREAUCRACY AT LEAST, AS MAJOR STABILIZING FACTORS, LIMITING INDIA'S PROPENSITY TO PRESSURE NEPAL AND PROVIDING ESSENTIAL RESOURCES TO A FLAGGING DEVELOPMENT EFFORT. THE PROMINENCE WHICH WAS GIVEN TO ASSISTANT SECRETARY ATHERTON'S CONGRESSIONAL REMARKS IS INDICATIVE OF THE NEPALESE DESIRE TO FOCUS PUBLIC ATTENTION ON THE SUPPORT OF FRIENDLY POWERS AND PARTICULARLY ON THE US COMMITMENT TO NEPAL'S INDEPENDENCE AND ECONOMIC DEVELOPMENT. AS THE CORONATION APPROACHES AND WITH THE PROSPECT OF A HIGH LEVEL U.S. DELEGATION, WE CAN ANTICIPATE FURTHER POSITIVE COMMENTS ABOUT OUR ROLE. THE ONLY MODEST CLOUD ON THIS HORIZON IS SOME NEPALESE CONCERN ABOUT THE IMPLICATIONS OF IMPROVED INDO/U.S. RELATIONS AND OUR ACCEPTANCE OF INDIA'S PARAMOUNT ROLE IN THE SUBCONTINENT. THEY WILL BE WATCHING CAREFULLY THE EVOLUTION OF OUR RELATIONS WITH NEW DELHI AND WILL ALWAYS WELCOME A REAFFIRMATION OF THE PROPOSITION THAT OUR RELATIONS WITH NEPAL ARE NOT DEPENDENT ON OUR RELATIONS WITH INDIA.

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Message Attributes

Automatic Decaptioning: Z
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: FOREIGN RELATIONS, POLITICAL SITUATION, CENTRAL GOVERNMENT, CIVIL DISORDERS
Control Number: n/a
Copy: SINGLE
Draft Date: 06 NOV 1974
Decaption Date: 28 MAY 2004
Decaption Note: 25 YEAR REVIEW
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: KelleyW0
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1974KATHMA04540
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Film Number: D740319-1032
From: KATHMANDU
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1974/newtext/t19741167/aaaaceub.tel
Line Count: 545
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION NEA
Original Classification: CONFIDENTIAL
Original Handling Restrictions: LIMDIS
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 10
Previous Channel Indicators:
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: LIMDIS
Reference: KATHMANDU 2953
Review Action: RELEASED, APPROVED
Review Authority: KelleyW0
Review Comment: n/a
Review Content Flags:
Review Date: 11 JUN 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <11 JUN 2002 by boyleja>; APPROVED <27 MAR 2003 by KelleyW0>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: NEPAL: CURRENT SITUATION
TAGS: PFOR, PINS, NP, US
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005